MAINE DEVELOPMENT FOUNDATION

The Maine Consumer: Under Pressure

Submitted to:

Central Maine Power

Central Maine Power Company

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About the Authors

Laurie G. Lachance – President and CEO

Laurie was named President of the Maine Development Foundation in 2004 and is responsible for overseeing all the activities of the foundation. Prior to coming to MDF, Laurie served as the Maine State Economist for eleven years for three governors. In that capacity, she chaired the Maine State Revenue Forecasting Commission, and served as lead or co-lead on utility restructuring, telecommunications, the retirement industry, and tax reform. Prior to joining the state government, Laurie served as the Corporate Economist at Central Maine Power Company. She is a frequent author and speaker on the economic status of Maine. Laurie holds an undergraduate degree from Bowdoin College and an MBA from Thomas College.

Patricia H. Hart – Senior Program Director

Patricia joined MDF in 2008 as the Senior Program Director of the Maine Employers' Initiative, an initiative to increase educational attainment among Maine's adult workforce. Prior to joining MDF, she operated her own consulting practice for ten years providing economic analysis, program evaluation and research consulting to clients in energy, economic development, health, education and social service fields. Patricia has a B.A. in Economics and Classical Studies from the College of William and Mary and an M.S. in Resource Economics from the University of Massachusetts.

About Maine Development Foundation

The Maine Development Foundation (MDF) is a private, non-partisan, non-profit 501(c)(3) corporation created by the Governor and Maine State Legislature in 1978 with a broad mandate to promote the economy. MDF drives sustainable, long-term economic growth for Maine. MDF stimulates new ideas, develops leaders, and provides common ground for solving problems and advancing issues.

Maine Development Foundation

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Overview

Maine is currently in one of the deepest economic downturns it has ever experienced, and, as a result, Maine consumers are under considerable pressure to make ends meet. What started as a normal dip in a business cycle in 2007 and early 2008 turned into a deep drop in many state and national economic measures by the end of 2008. The drop was a result of an unprecedented confluence of events, including: an increase in commodity prices, primarily oil and food, to record high levels; problems in the financial sector due to the performance of subprime loans and mortgage backed securities; unsustainable housing values; and a consumer-driven economy with an over-reliance on credit. On the national level, many analysts are comparing the steep decline to the Great Depression of the 1930s, noting the recent increase in bankruptcy filings and the government bailouts of the nation's automakers and financial institutions. These factors led to a broad-based recession across the nation and in Maine that has affected all sectors of the economy – putting a squeeze on businesses, government agencies and consumers alike.

Table 1 shows the short-term changes in key economic indicators demonstrating the effect of the economic slowdown on Maine consumers and businesses in the last year. The changes over the last 12 months include:

- Unemployment, currently at 8.4%, is at its highest point in 18 years, after 13 years of staying below 5.5%.
- Total employment declined by 3% with a loss of 20,000 jobs.
- Maine state government, one of the state's largest employers, and many other businesses cut salaries, reduced benefits and mandated furlough days to close growing revenue and cost gaps.
- Bankruptcy filings increased by 33%, with an additional 1,000 Maine businesses and individuals declaring that they could not meet their creditor obligations.
- The rate of property foreclosures in the state increased from 1 in every 2,684 homes to 1 in 1,712 homes, a 58% increase.
- Credit card defaults, nationwide, increased 38% with close to 7% of all credit card balances in extreme default status.
- The proportion of Maine people receiving support through the Maine Supplemental Nutrition Assistance Program (food stamps) increased 18%. The program currently covers 214,542 of Maine's 1.3 million residents, approximately 16% of the total population.

In addition to these hardships, Maine's residents have been struggling for years to extend their below average personal incomes to make payments for essential goods and services that have very high costs. These goods and services include:

- The volatile cost of oil - 85% of Maine residents are dependent on oil products to heat their homes.
- Maine residents and businesses pay some of the highest electricity prices in the nation.
- From 2000 to 2007, housing became less affordable in Maine. On average, housing takes a greater share of income in Maine than for households across the nation.
- Health-care expenditures in Maine have grown at a rate much faster than the U.S. and based on national predictions will continue to grow at a faster rate.
- Maine state and local tax payments relative to income continues to be among the highest in the nation.

Table 1. Change in Key Economic Indicators, July 2008 to July 2009

Indicator	July 2008	July 2009	% Change
U.S.			
CPI	219.96	215.35	-2%
Credit Card Defaults	4.82%	6.7%	38%
S&P 500 Adjusted Closing Index	1,267	987	-22%
Maine			
Bankruptcy (12 mo. moving total)	2,684	3,578	33%
Foreclosure Rate (1/every x housing units)	2710	1712	58%
Unemployment Rate	5.4%	8.4%	49%
Wage & Salary Employment (1,000s)	617.7	596.71	-3%
Taxable Auto Sales ($s)	$3,653,010	$3,201,308*	-12%
Taxable Building Supply Sales ($s)	$2,392,805	$2,111,510*	-12%
Consumer Price Index for Food	214	221	3%
Supplement Nutrition Assistance Program (people)	181,814	214,542	18%

*June 2009 data

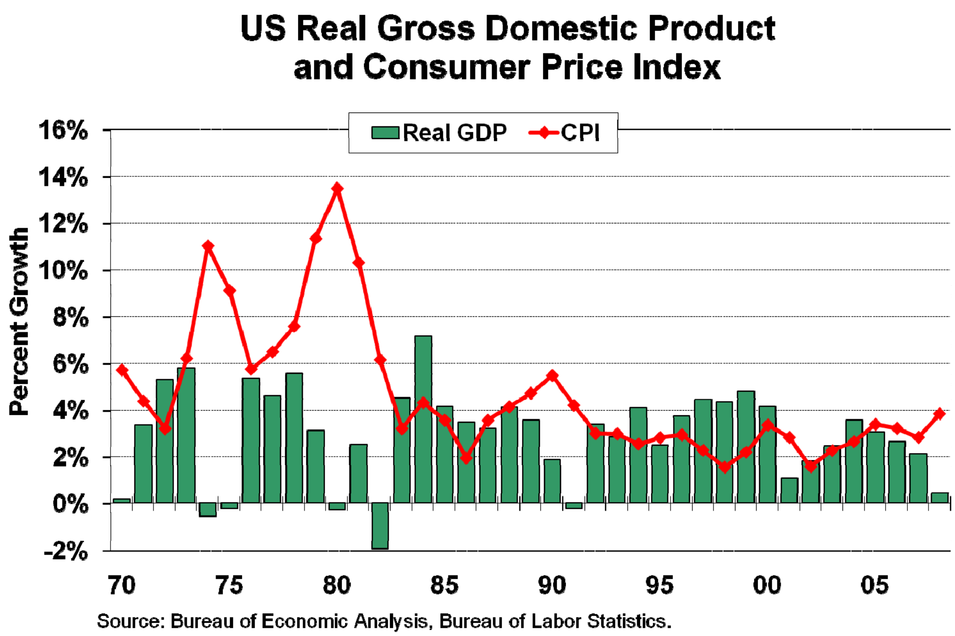
Coupling the impacts of the current recession with the Maine consumer's already weak economic standing has led to unprecedented pressures on households and businesses to make ends meet. Not only has the Maine consumer's income taken a hit, but their purchasing power has eroded and, perhaps even more importantly, their confidence has been badly shaken. As is shown in key economic indicators for Maine and the U.S., the impacts of the recession have been felt acutely over the past twelve months.

The following economic brief shows the trends in national and state-level economic indicators and discusses the impact of the recession on Maine residents and businesses.

National Economic Backdrop

After enjoying three years of recovery from the relatively mild recession of the early part of this decade, national economic growth began showing signs of slowing in late 2005 and the slowdown accelerated in 2008. Economic growth is measured by the change in the real Gross Domestic Product (GDP), the value of all goods and services produced. See Figure 1. The downturn came as a reaction to the combination of three unforeseen events: skyrocketing oil prices, rising food prices and the crisis in the financial markets. By year end 2008, the National Bureau of Economic Research economists officially declared that the U.S. was in a full-fledged recession, defined generally as a drop in real GDP for two consecutive quarters. Also during this time, inflation began to creep up, rising to the highest levels seen since 1991.

Figure 1



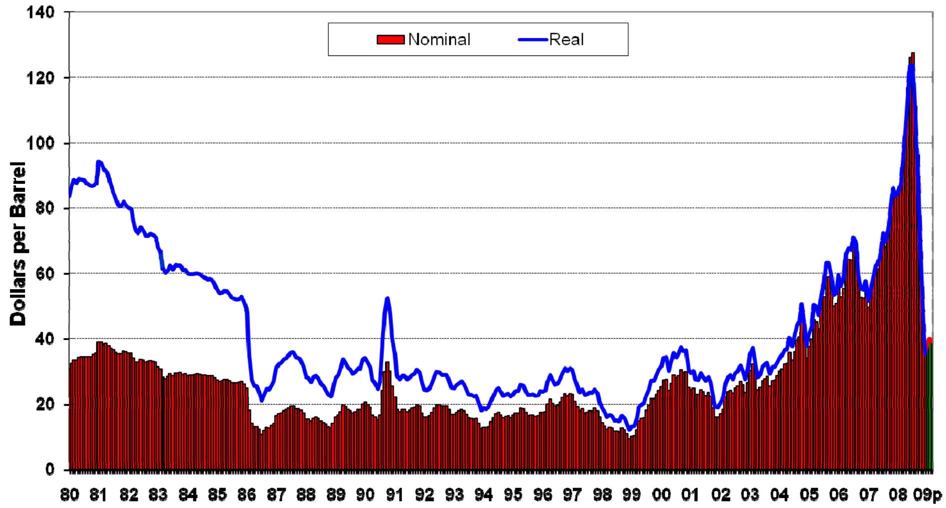
For a petroleum dependent nation like the U.S., the unprecedented run-up in nominal and real crude oil prices in 2007 and 2008 dealt a severe blow to industry and households, increasing costs for production and delivery of almost all goods and services. Real oil prices, at their peak, were 30% higher than the levels seen during the oil crisis of the early 1980s. See Figure 2.

In July 2007, crude oil was \$70 per barrel; by July 2008 prices reached \$126 per barrel, an 82% increase in a single year.

The effects of the high prices were felt in every sector of the U.S. economy as transportation, energy, manufacturing inputs, and basic costs of living rose rapidly.

Figure 2

Crude Oil Prices U.S. Average Real¹ and Nominal Prices
Monthly, January 1980-March 2009



[1] In chained (2000) dollars, calculated by using gross domestic product implicit price deflators. 2009 data points are projections.

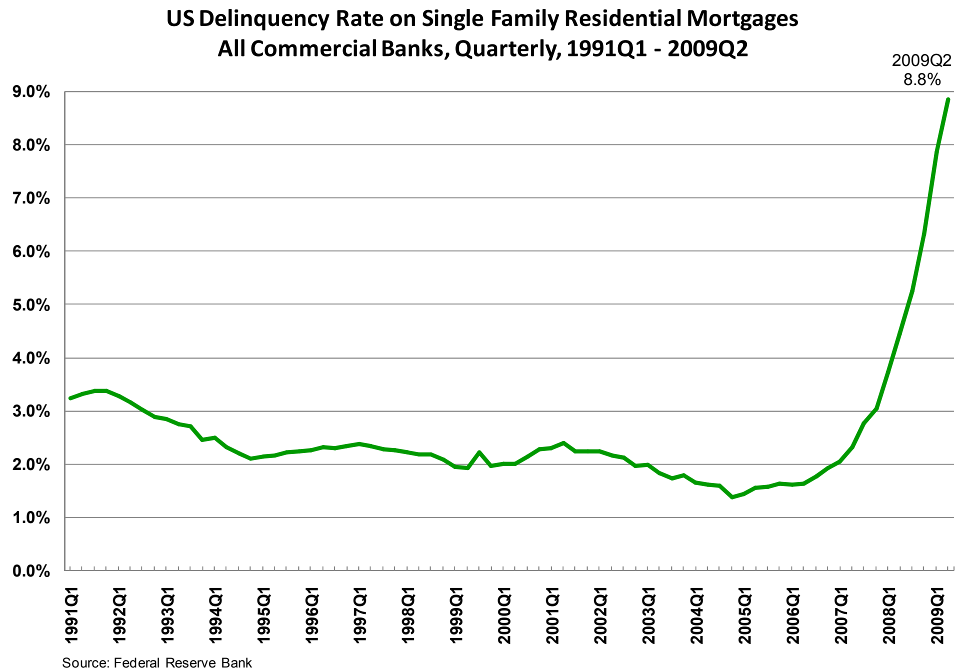
Source: Energy Information Administration.

Added to the rising costs of oil products, the U.S. Department of Agriculture, Economic Research Service reported that food prices also increased 15% from 2005 to 2009. The price increases were due to the increase in oil prices, drought in key producer regions and a mix of socio-political factors including a greater demand for grains used to make bio-fuel and population growth. Worldwide shortages in commodities such as rice and corn caused extreme hardship on countries whose diets rely on these staples. As a result, in the U.S., prices increased markedly for some consumer products in 2008, particularly for cereal, bakery products, fats and oils, and eggs which each experienced double-digit cost increases.

Unlike other recessionary periods, in recent decades, more consumers relied on credit to support their lifestyles. Credit cards were easy to obtain, mortgage companies had relaxed loan eligibility requirements and most people purchased essentials, such as personal vehicles, on credit. When oil prices spiked, consumers' discretionary income dropped, leaving them with diminished resources to make credit and loan payments. By mid-2006, U.S. delinquency rates on mortgages, consumer loans and credit cards started to rise rapidly. In fact, national delinquency and foreclosure rates are now at record high levels. In the last year alone, the national delinquency rate for all loans doubled from 3.37% in June 2008 to 6.49% in June 2009.

Delinquencies were seen much more prominently among consumers loans secured for housing, for credit cards and other loans. As of the second quarter of 2009, 8.84% of all loans on residential properties were delinquent, defined as having payments past due 30 or more days. See Figure 3. The current delinquency rate is the highest on record and has doubled in the past 12 months, from 4.45% in June 2008 to 8.84% in June 2009. The previous record-high rate was 3.36% in 1991.

Figure 3



By the end of the 2nd Quarter of 2009, 4.92% of consumer loans were delinquent; up from 3.59% for the 2nd Quarter of 2008. See Figure 4. A higher proportion of credit card loans fell into delinquency with 6.7% of all credit card loans delinquent as of the end of the 2nd Quarter of 2009, a 33% increase since June 2008. See Figure 5. In response to this situation, banks and other lenders have tightened their lending practices, making it more difficult for everyone, consumers and businesses, to qualify for credit. The credit crunch has impacted even the most credit-worthy businesses making it difficult for them to purchase inventory and meet payroll.

Figure 4

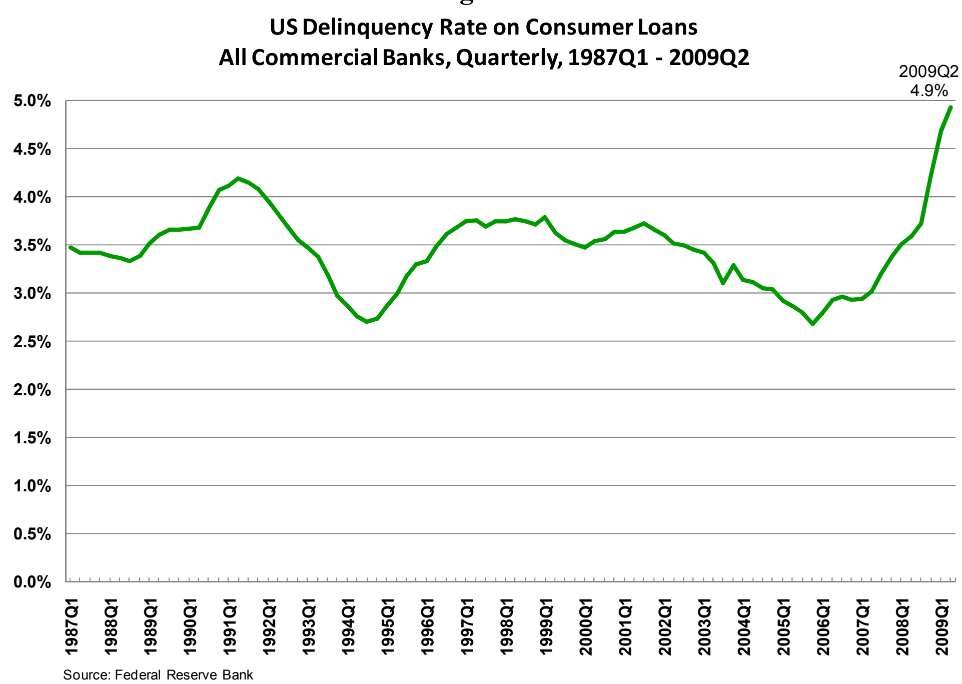
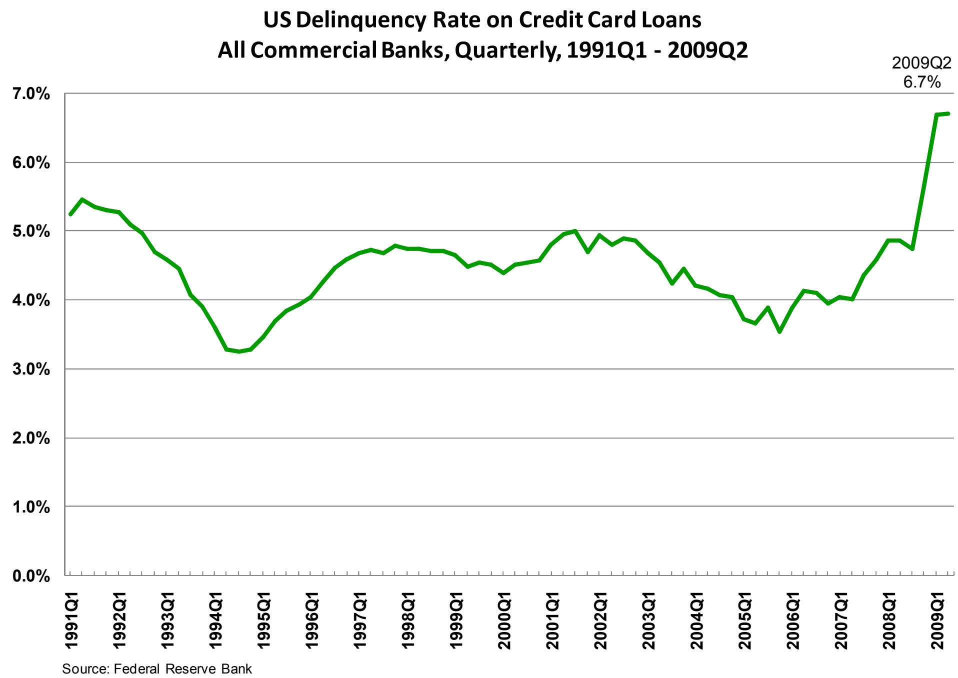
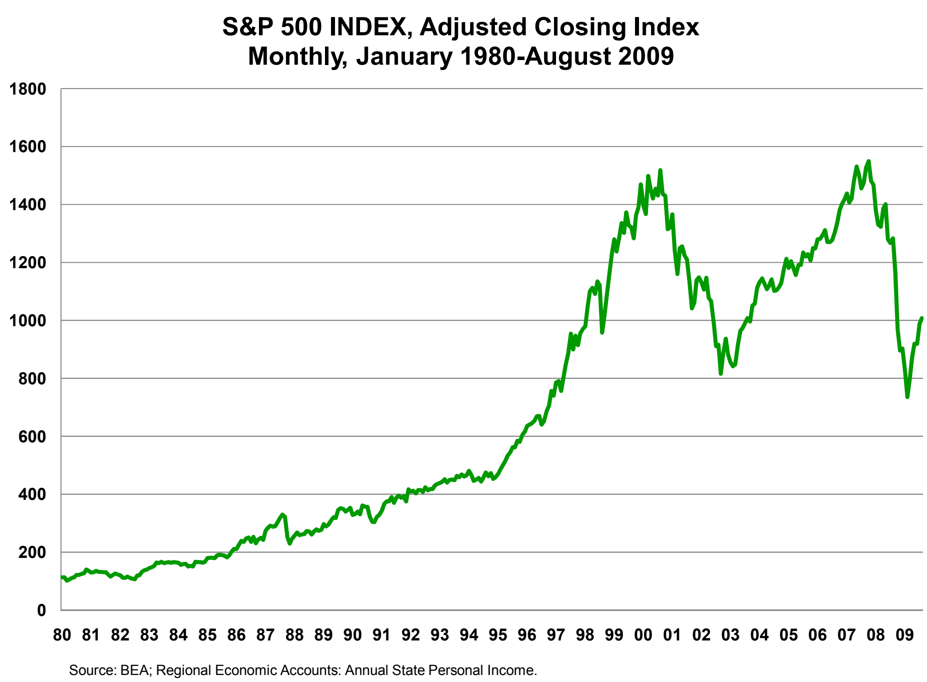


Figure 5



The combined influence of the drop in GDP, increase in oil prices, and crisis in the financial markets led investors to lose confidence and pull out of the stock market. The ultimate result in the loss of confidence in the strength of the economy translated to a 50% decline in the stock market indexes from mid-2008 to early 2009.

Figure 6

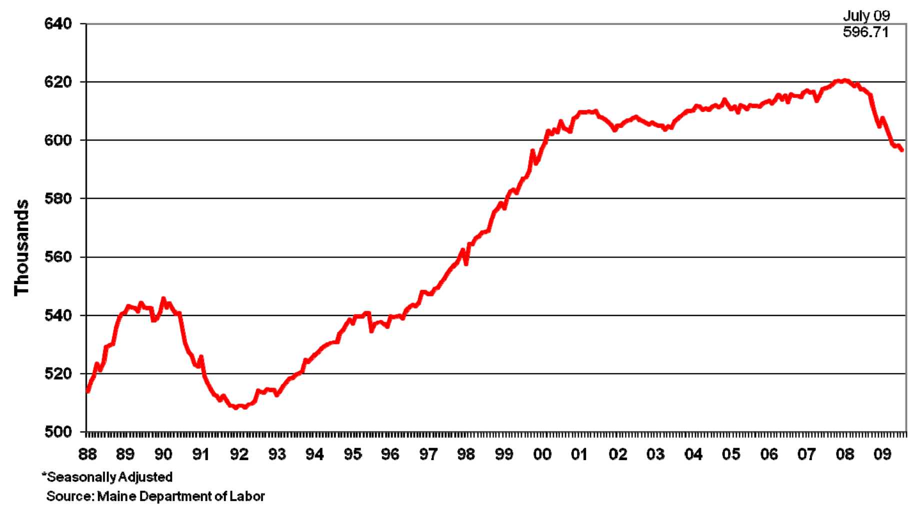


Maine's Economic Condition

Since the start of the recession, Maine's measure of Wage and Salary Employment has experienced a precipitous fall from a high of 620,000 workers in early 2008 to the July 2009 level of 596,000. This drop of over 24,000 workers represents about 4% of the previous high point. Of those job losses, 20,000 occurred in the last 12 months from June 2008 to June 2009. While it is too early to predict how much longer Maine will continue to have losses in employment, at the current pace, the state is on track to equal the losses sustained in the downturn of the early 1990s. At that time, roughly 35,000 jobs were lost representing a 6.5% loss on an even smaller employment base.

Figure 7

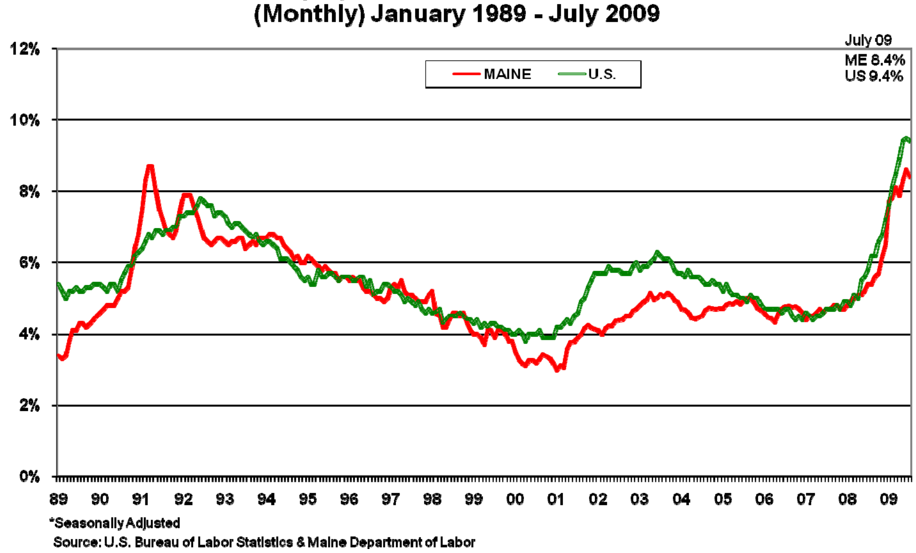
Maine Wage and Salary Employment*
(Monthly) January 1988 - July 2009



As a result of the drop in total number of jobs, unemployment rates in Maine and the nation have climbed sharply over the past 12 months from the 5% level in June 2008 to 8.4%. While Maine joblessness remains below U.S. levels of 9.4%, both have surpassed the high rates experienced in the depths of the recessionary period almost two decades ago.

Figure 8

Unemployment Rates, Maine and U.S.*
(Monthly) January 1989 - July 2009



Income

Maine has the lowest level of per capita income in New England and ranks 33rd out of all 50 states on this measure. With per capita income of $35,381, Maine is 27% lower than the New England average of $48,715 and 11% lower than the U.S. average of $39,715. See Table 2 below.

Thus, the average household has less means than its neighbors in New England and than most households across the nation. Yet Maine households face similar, if not higher costs for many essential items.

Table 2. Per Capita Personal Income and National Rank, 2008 Preliminary, New England and U.S.

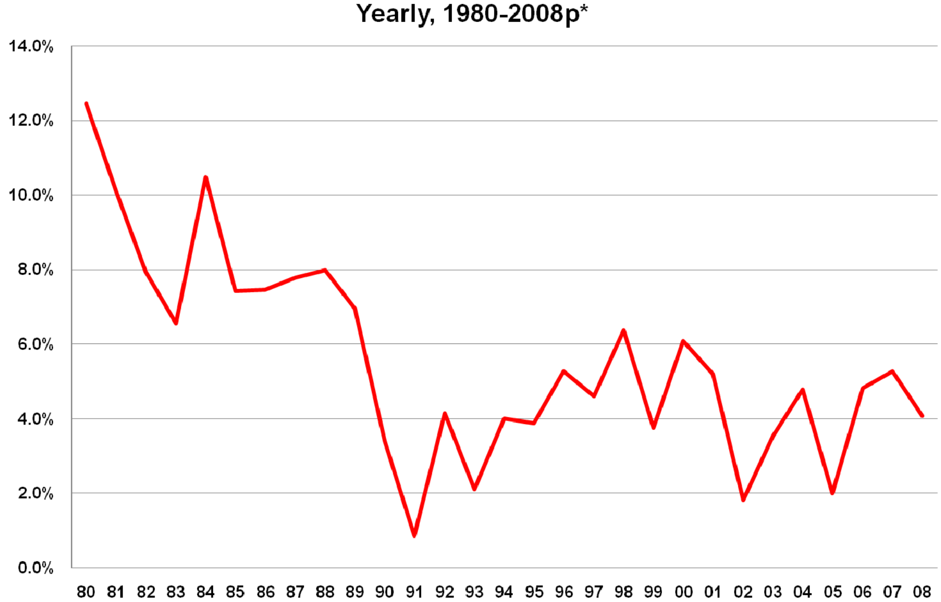
	Income	Rank
US	**$39,751**	
NE	**$48,715**	
CT	$56,248	1
MA	$50,735	3
NH	$42,830	9
RI	$41,008	15
VT	$38,880	22
ME	$35,381	33

Source: Bureau of Economic Analysis and U.S. Census

Maine consumers entered this recession at a significant disadvantage. Per capita income growth in Maine has never really shown the rebound from the early 1990s downturn that traditionally marks a recovery. As Figure 9 illustrates, per capita income growth, at its highest, was in the 4%-6% range, far different than the double-digit growth enjoyed during the booming 1980s. Even these relatively tepid gains began to slow through this decade, averaging more in the vicinity of 2%-4% in nominal terms. This offered little in the way of relief to Maine consumers once oil prices began to rise, out-stripping the meager income gains and eroding the purchasing power of households and businesses alike.

Figure 9

Per Capita Personal Income Growth in Maine Yearly, 1980-2008p*



* p = preliminary

Source: BEA; Regional Economic Accounts: Annual State Personal Income.

Relatively small income gains over the past two decades have resulted in Maine's national rank slipping from its all-time high of 28th in 1988 to the mid-30s where we have remained in a holding pattern for the better part of 20 years. See Figure 10.

What this means to Maine consumers is that they never make much headway in catching up and closing the gap that separates them, income-wise, from the consumers in other states. Figure 11 shows that Maine has closed the gap to within 8.5 percent of the US average during times of prosperity, but tends to slip back whenever economic conditions cool.

With below average incomes, rises in the cost of living hit harder and make Maine consumers more vulnerable to economic swings as there is less of a financial cushion to serve as a buffer.

Figure 10

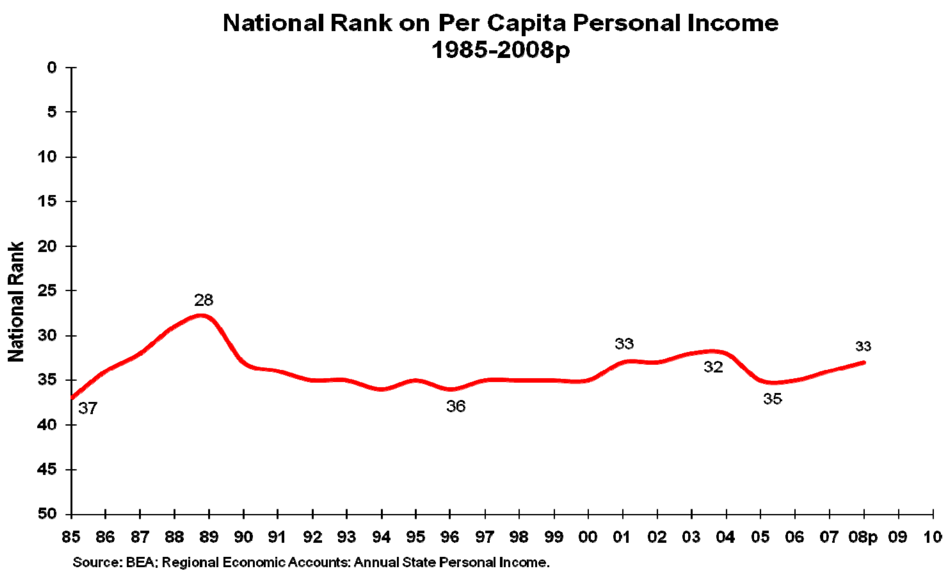
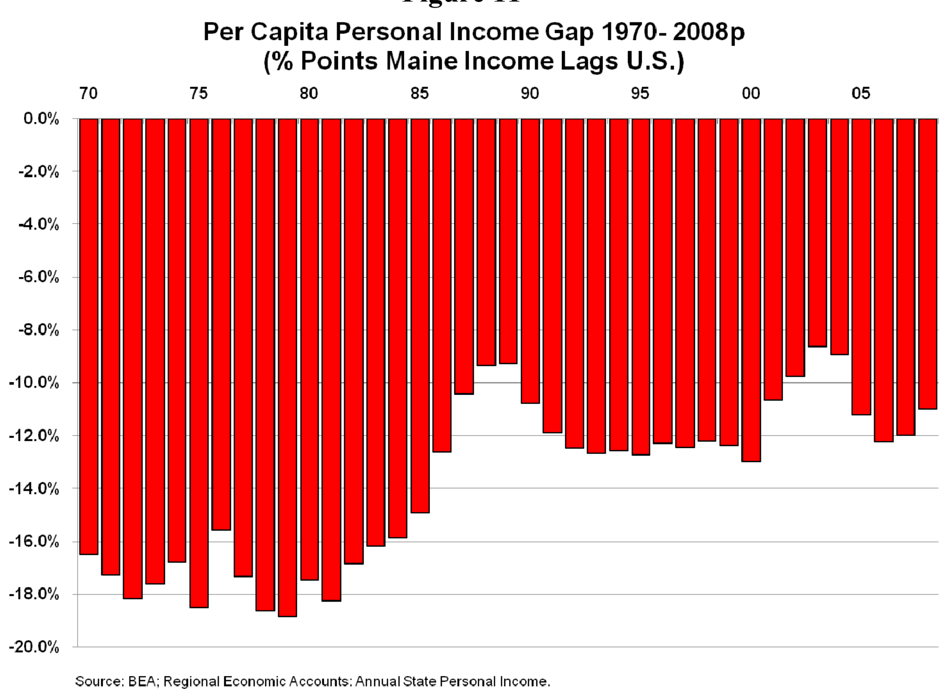
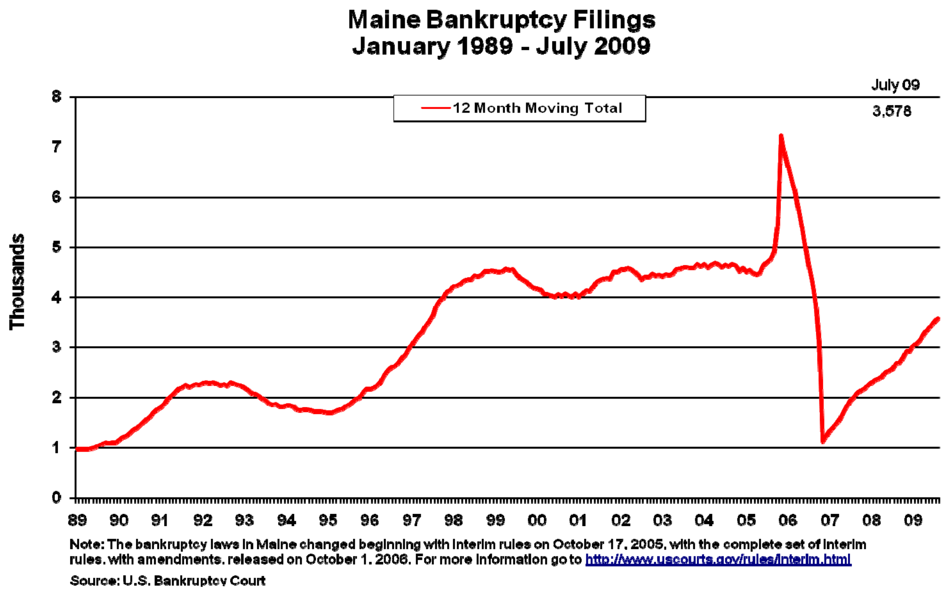


Figure 11



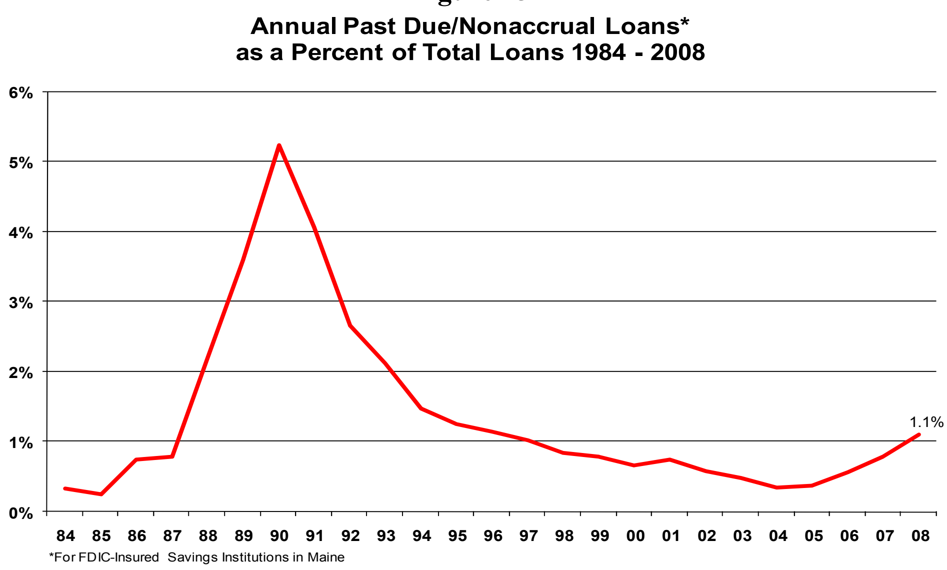
Bankruptcy filings are another indicator of financial stability for consumers and businesses. See figure 12. Maine bankruptcy filings, including Chapters 7, 11, 12 and 13, doubled during the deep recession of the early 1990s and, more troubling, doubled again through the recovery period that followed. A change in bankruptcy laws that went into effect in late 2005 led to a spike in filing activity before the new baseline level was established. Even with tighter restrictions, the number of filings has risen sharply since mid-2006, and the upward trajectory shows no signs of changing at this point.

Figure 12



Maine banks are starting to feel the pinch of their customers' financial issues as the percentage of past due/nonaccrual loans started to rise in 2008 according to Federal Deposit Insurance corporation data. See Figure 13. Bank leaders suggest that once 2009 figures become available, Maine will likely see a significant up-tick in this measurement. According to the Mortgage Bankers Association of Maine, the delinquency rate for single-family residential mortgages in Maine was 7.70% as of the end of the 4th Quarter of 2008. Foreclosures are also up dramatically with 3.49% of residential loans in Maine in the process of foreclosure and 5.65% of loans seriously delinquent (past due 90 or more days). Too many Mainers are faced with difficult decisions about which bills to pay this month.

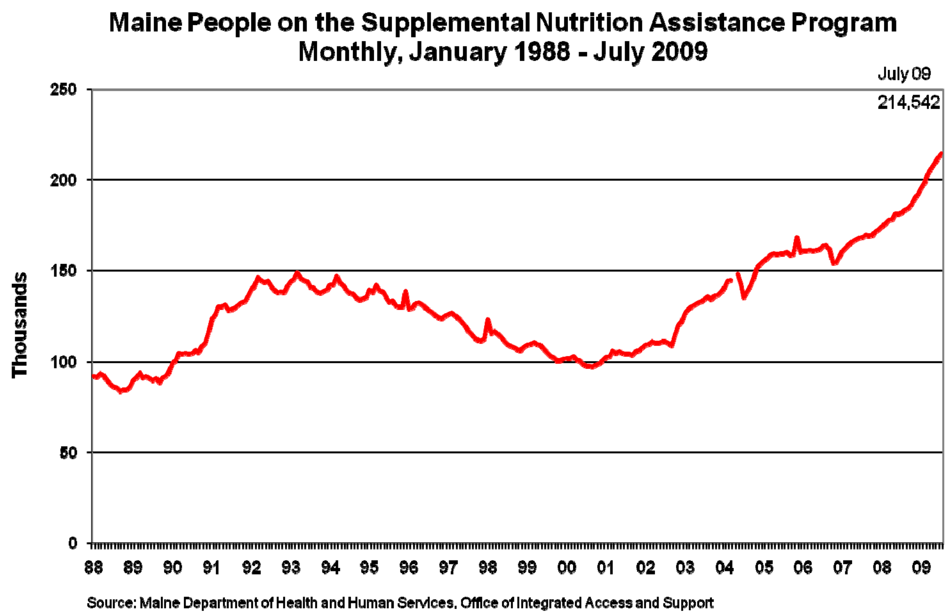
Figure 13



It appears that as economic conditions have worsened, a greater proportion of residents have been provided some form of government assistance. Figure 14 shows that about 16% of Maine's people are receiving food stamps through Maine's Supplemental Nutrition Assistance Program, a doubling in numbers since 2000 and an 18% increase from July 2008 to July 2009.

While social assistance numbers may not always reflect economic conditions because programmatic changes and marketing can affect participation, the numbers of Maine people on the Supplemental Nutrition Assistance Program do offer some insight into the portion of Maine's population living on the edge.

Figure 14

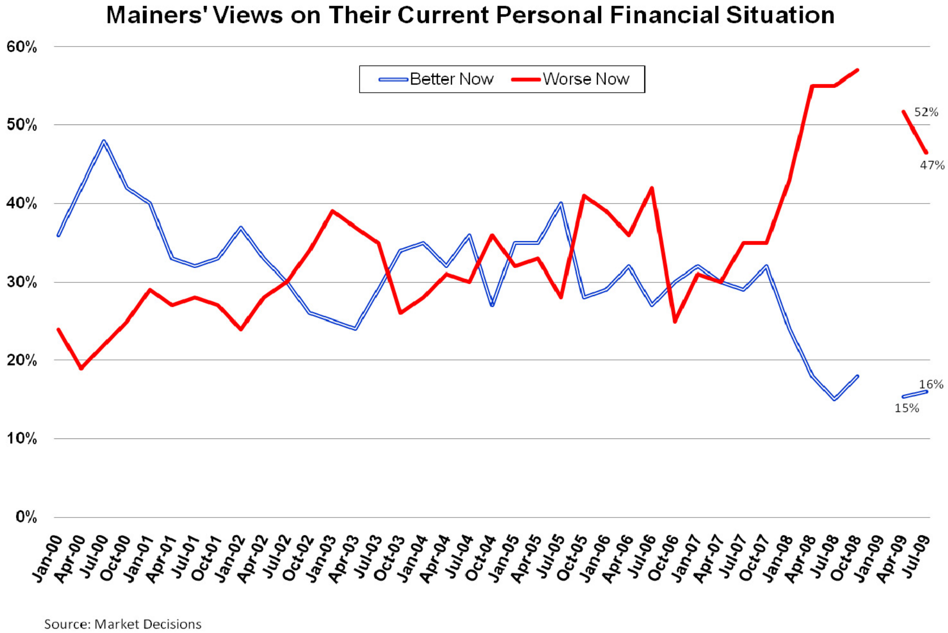


Consumer Confidence in Maine

As a result of lost wages and increases in product prices, consumers across the nation deferred purchases of durable goods and big ticket items such as vehicles, electronics, and new homes and even began to rethink the smaller day-to-day expenses such as eating out. Their collective withdrawal from retail markets was felt in all sectors including retail, manufacturing, service, delivery and support industries such as printing and packaging. After enjoying decades of credit fueled spending as well as strong confidence from the wealth effect of a growing stock market, consumers rethought their purchasing behaviors and started to go without items that were once thought to be necessities.

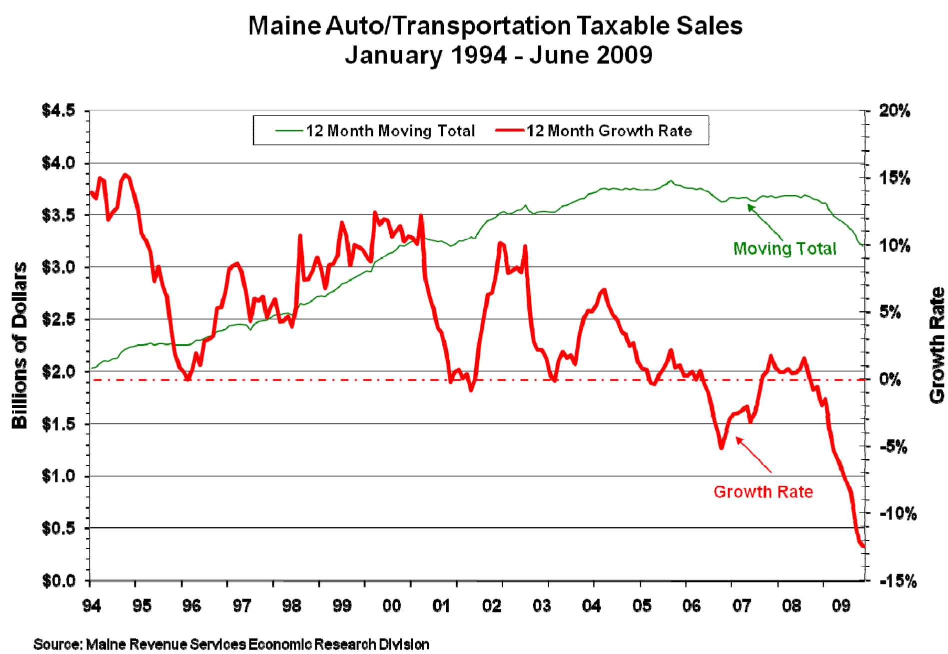
When Market Decisions, a Maine-based market research firm, surveyed consumers over the 2007 through 2009 timeframe, respondents were clearly uneasy about their current and future personal financial conditions. As Figure 15 illustrates, from late 2006 to late 2008, when consumers were asked if their current personal financial situation was better or worse now, the percentage responding "worse" jumped from under 30% to nearly 60% through Fall of 2008. At the same time, the percentage of those responding "better" fell from 30% to under 20%. While the most recent poll findings show a change in consumer confidence in the positive direction, the overall confidence levels remain low.

Figure 15



Evidence of the erosion in consumer confidence began surfacing in Maine retail markets as early as 2006 with an actual decline in auto sales which recovered briefly in late 2007 and early 2008 before beginning its rapid and precipitous descent. Since June 2008, sales have dropped by 12.5%. See Figure 16.

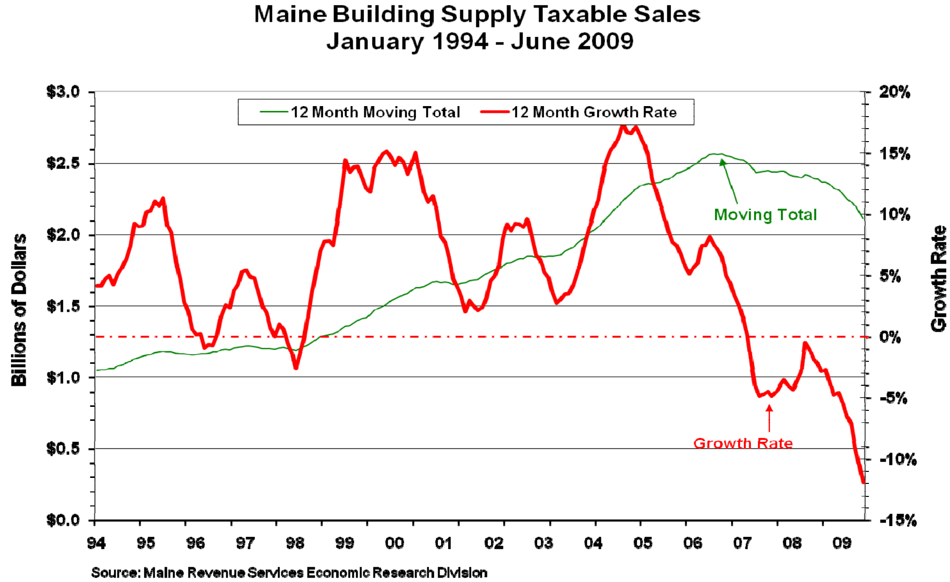
Figure 16



Building-supply taxable sales provide another insight into the relative confidence of Maine's consumers. Building-supply sales began to slow significantly through 2005 and 2006, but did not show a decline until early 2007.

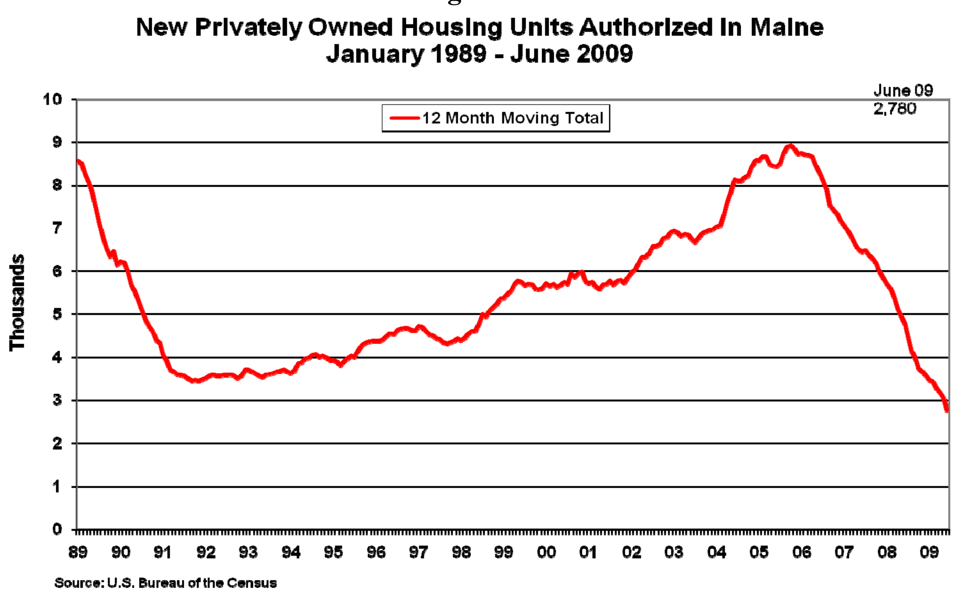
Growth in these sales has remained negative for two and a half years, with a significant acceleration, 12%, in the rate of decline from late 2008 to present. This leading indicator shows no signs of turning around soon.

Figure 17



Similarly, the number of new, privately owned housing units authorized in Maine began dropping in early 2006 and declined at a pace that was virtually identical to the early 1990s during the collapse of the regional housing market in New England. While the number of housing units authorized in earlier recessionary periods bottomed out around 3,500, the current decline has gone below the 3,000 mark and does not yet appear to have abated as of June 2009.

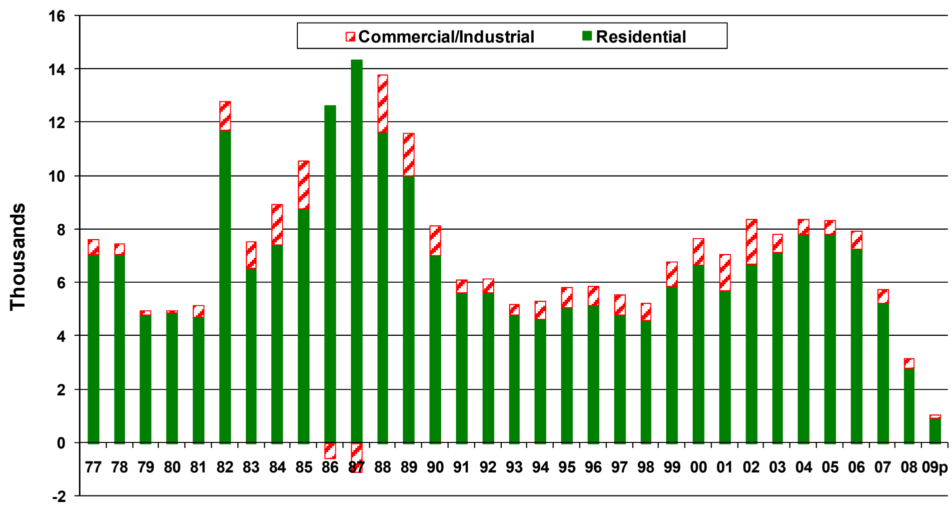
Figure 18



Another indicator of both consumer confidence and current economic conditions is the gain in Central Maine Power Company's residential and commercial and industrial customer base. Since CMP serves roughly 80% of Maine's economy, it provides an indication of vibrancy in both the residential and business sectors. As Figure 19 illustrates, customer gains have slowed considerably and during 2009, fell to the lowest levels seen in decades – providing another indication of the severity of the current period.

Figure 19

Central Maine Power Annual Gain in Customers 1977 - 2009p*



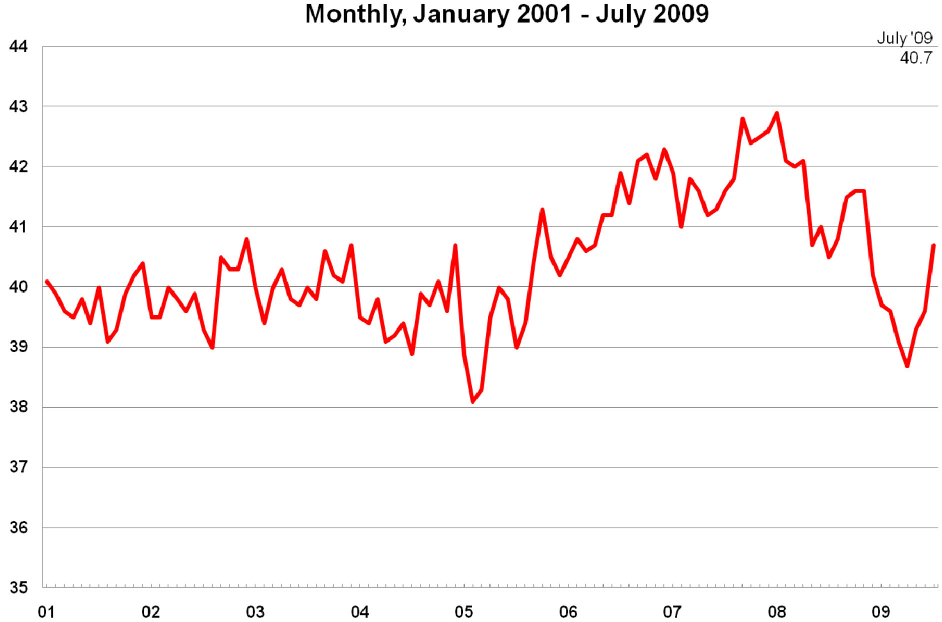
* 2009 is an estimate.

Source: Central Maine Power Company.

Another indicator of economic activity that tends to lead the business cycle is Manufacturing Hours Worked. As can be seen below, hours worked had been relatively stable through the first half of the decade, rose through much of 2006 and 2007, then began to drop through 2008. During the last year, manufacturing employment dropped 3% translating to a loss of wages for hourly workers. The most recent reports show that manufacturing hours may be increasing; however, this includes only active industry and does not reflect the businesses that have shut down during this time period.

Figure 20

Maine Manufacturing Workers Average Weekly Hours Worked Monthly, January 2001 - July 2009



Source: US Bureau of Labor Statistics

Cost Pressures

As discussed earlier, Maine people have incomes below the U.S. average. In addition, Maine residents and businesses face some of the nation's highest costs for essential goods and services, further squeezing individual and business budgets. Combined, these conditions mean that, when a recession hits, they are more vulnerable to its impacts.

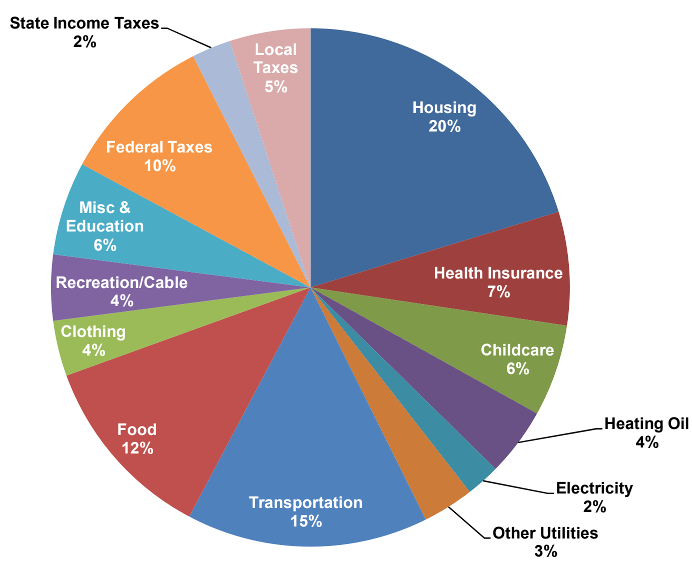
According to analysis of consumer spending conducted by Patricia H. Hart in 2008, *The Average Maine Household Struggles to Balance Its Budget*, over three-quarters of the annual spending for a typical Maine family in 2006 went to:

- Housing (20%)
- Taxes (17%)
- Transportation (15%)
- Food (12%)
- Health Insurance (7%)
- Heating Oil and Electricity (6%)

The report notes that for each of these spending categories, Maine residents face costs that are above national averages. For example, health insurance premiums for a typical family of three are 12% higher than national averages. Electricity prices are higher, energy needs are greater in the cold climate and so total costs are typically 6-10% higher than households across the nation. Moreover, when oil prices spiked in 2008, Maine homes heated with oil experienced an additional $2,158 increase in energy costs compared to a $126 increase for home heating nationally. At the same time, Maine consumers have lower incomes to pay these non-discretionary bills. Moreover, in some cases, like energy, transportation, and food, costs have increased since the 2008 report, further crowding out the consumer's ability to pay for other necessities.

Figure 21

Annual Spending for a Typical Maine Family* in 2006



* 3 persons (2 adults, 1 school age child) with median income of $43,439 accoriding to the American Community Survey.

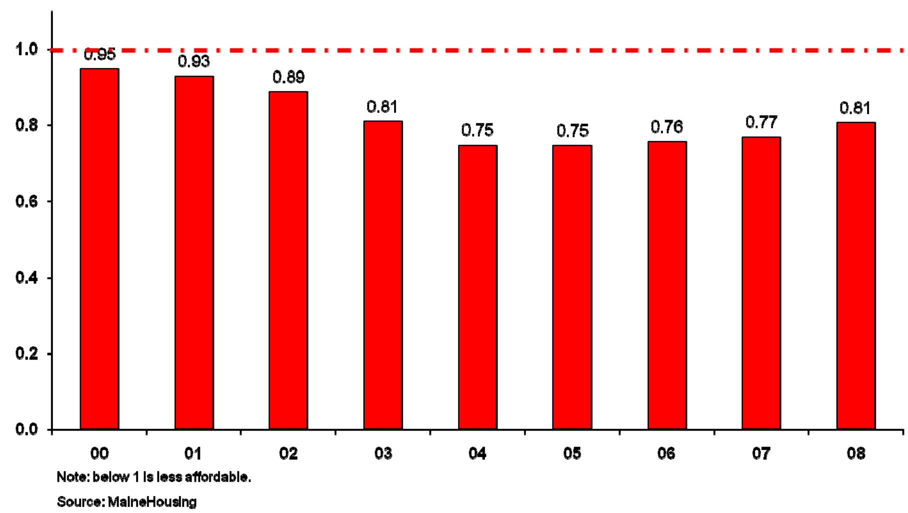
Source: Patricia Hart, The Average Maine Household Struggles to Balance Its Budget, June 2008 Update, Maine Public Spending Research Group

Figure 22 shows that housing affordability in Maine has eroded significantly this decade, further reinforcing the fact that Maine incomes have not kept pace with rising housing costs. Low housing affordability creates a drag on the economy and decreases disposable income. In many of Maine's employment centers, high housing costs are forcing people to commute long distances because they cannot afford to live in the same communities in which they work. This then increases their commute costs.

The Maine Economic Growth Council's 2009 report, *Measures of Growth*, reinforces these findings by analyzing county-level data. In 2000, 13 of Maine's 16 counties were considered affordable. By 2007, only three counties, Aroostook, Somerset and Piscataquis, had average housing prices in line with average incomes.

Figure 22

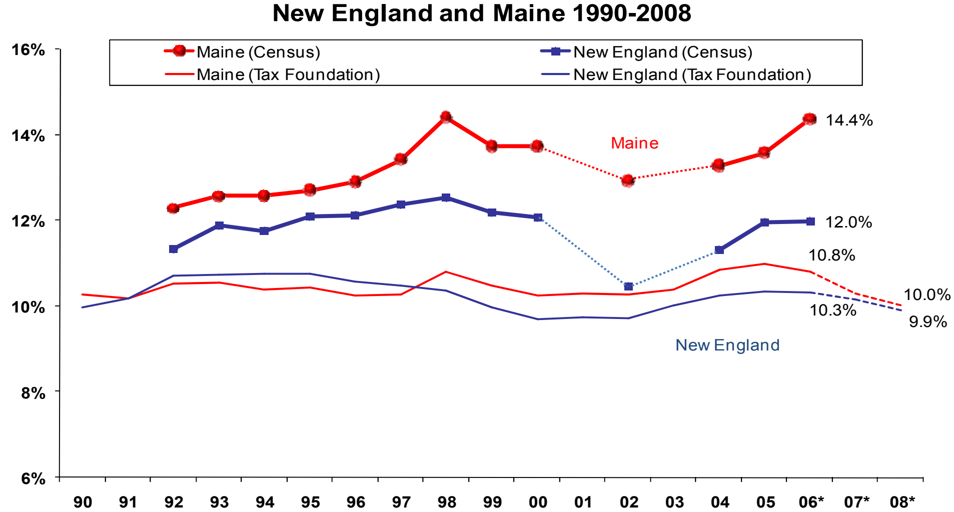
Housing Affordability in Maine (weighted owner/renter)
Yearly, 2000 - 2008



Along with many indicators of economic progress, the Maine Economic Growth Council's 2009 report also shows that the State and Local Tax Burden in Maine, using both the Census estimates and those of the Tax Foundation, is significantly above regional averages, further emphasizing the strain on consumers.

Figure 23

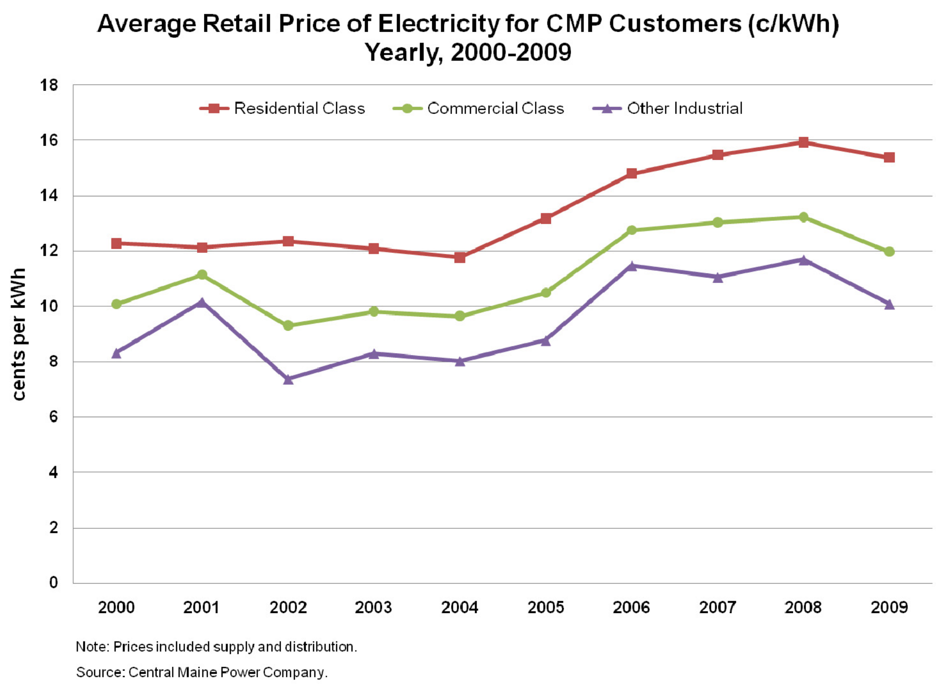
State and Local Taxes as a Percent of Income
New England and Maine 1990-2008



Source: US Census Bureau, The Tax Foundation.

The total price of electricity for Central Maine Power Company's customers across all sectors and customer classes rose significantly from 2002 through 2008, with the supply costs tracking the increases in oil prices. Recent supply costs have shown some decrease, leading to slightly lower total prices for consumers.

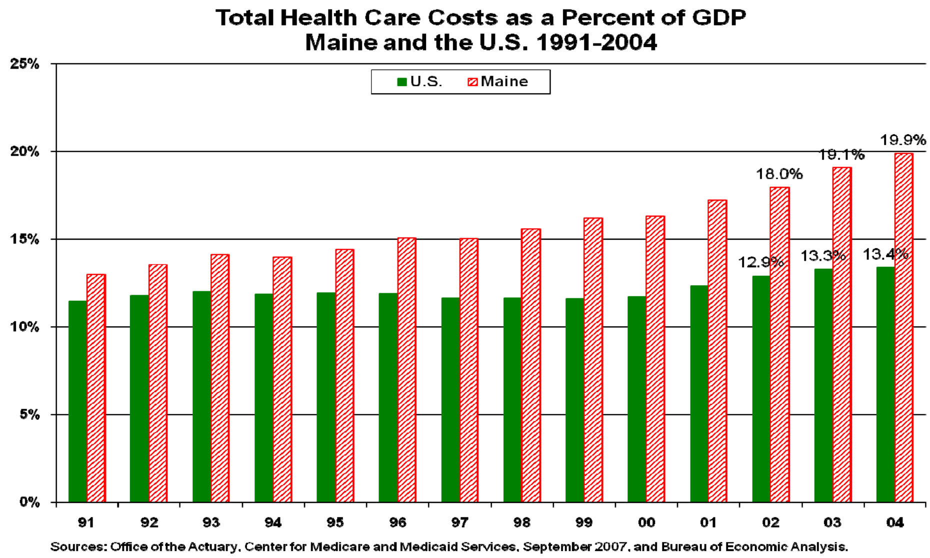
Figure 24



Health care has also grown more and more costly in recent decades. According to the most recent figures available to the Maine Economic Growth Council, the cost of health care in Maine started to separate from the U.S. average in the early 1990s, and by 2004 had grown to represent 19.9% of total state GDP while nationally the percentage was only 13.4%. See Figure 25.

Although new state-level data is not available beyond 2004, national data allows for estimates through 2007. The federal Center for Medicare and Medicaid Services (CMS) estimated that national health care spending was 16.3% of national GDP in 2007. By 2017, it is forecasted that national health care expenditures will reach $4.3 trillion or 19.5% of national GDP. Annual spending on a national level is forecasted to grow at a higher rate than GDP and inflation for the next decade. Based on the relationship in the graph, health care costs in Maine will likely continue to grow at a higher rate than GDP growth and represent an ever increasing share of the economy for the same period.

Figure 25



Finally, in addition to Maine residents and businesses facing above average costs for some of their essential and non-discretionary expenditures such as housing, taxes, and health care, Maine people are also highly dependent on petroleum products for both transportation and heating needs. In the transportation sector, approximately 85% of all freight moves by truck and 95% of all passenger travel is by car, which means that increases in diesel and gasoline prices hit Maine people very hard. In addition, roughly 89% of Maine households use some form of petroleum product to heat their homes in the winters, meaning that when heating fuel prices increase, Maine residents are at risk.

As Figures 26 and 27 highlight, the average prices of both gasoline and heating oil increased more than 70% from July 2007 to July 2008, with real prices exceeding the levels experienced during the energy crisis of the early 1980s.

Figure 26

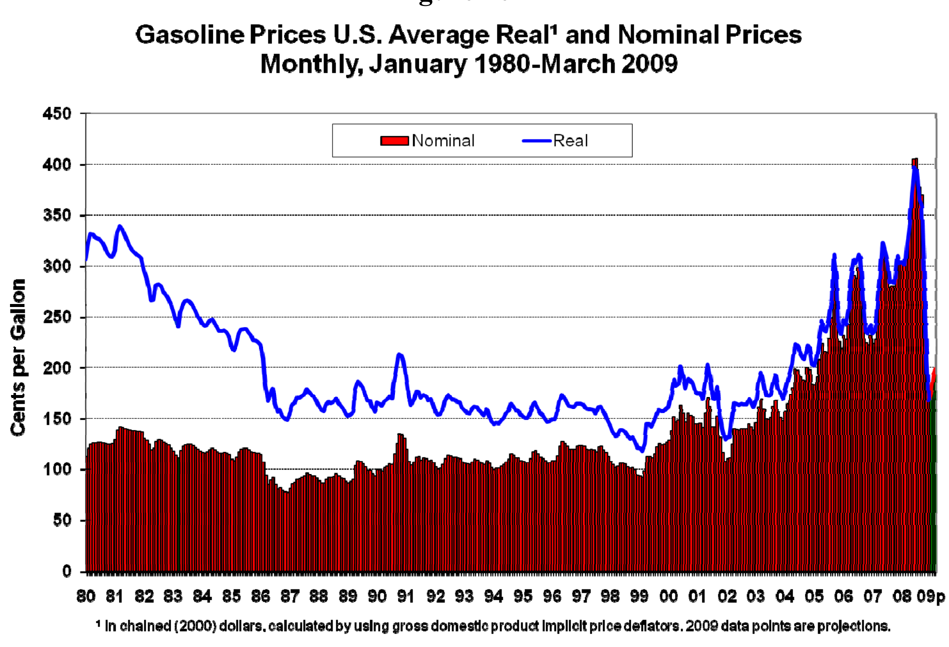
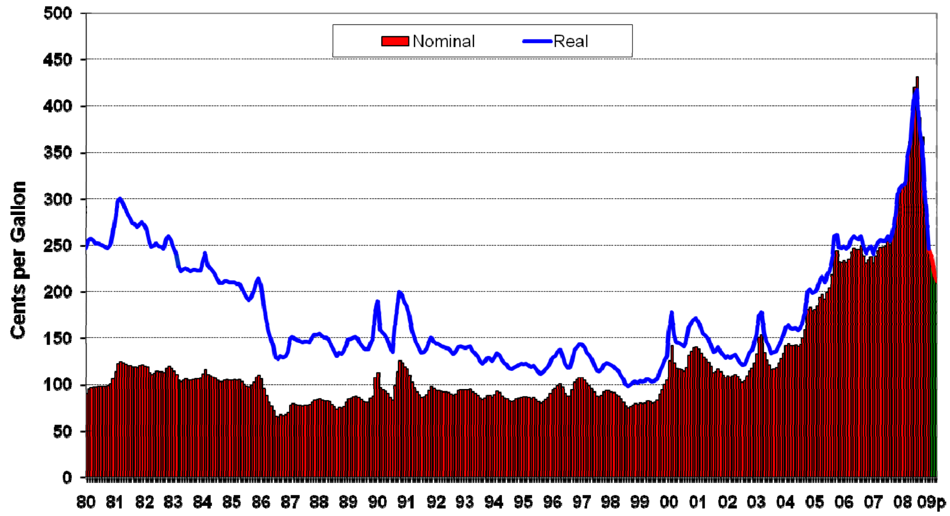


Figure 27

Heating Oil Prices U.S. Average Real[1] and Nominal Prices
Monthly, January 1980-March 2009



[1] In chained (2000) dollars, calculated by using gross domestic product implicit price deflators. 2009 data points are projections.

Source: Energy Information Administration.

Conclusion

For the past two to three years, Maine consumers have been, and continue to be, under enormous financial pressure. Facing the convergence of relatively low and eroding incomes, relatively high costs for essential goods and services and, in some cases, overwhelming debt, consumers and businesses are struggling to make ends meet. As is seen by the rising delinquency and foreclosure rates, unfortunately, many have shown they cannot withstand the burden. While the economic pressures built up over time, the impact on Maine's consumers has been felt acutely in the past 12 months:

- The unemployment rate reached a 20 year high at 8.4%, a 49% increase over the previous twelve months.
- Maine property foreclosure rates increased by 58%.
- Bankruptcy rates in the state increased 33%.
- Auto sales and building supply sales dropped 12%.
- The proportion of people receiving support from the Supplemental Nutrition Assistance Program (Food Stamps) increased 18%, now covering more than 200,000 Maine residents.

Until economic growth resumes and household budgets begin to see some relief, the pressure will continue, forcing Maine people to make extremely difficult decisions about what they purchase and which bills they pay.

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